



Islamic Development Bank

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Islamic Development Bank

Sukuks

Alternative Asset Classes

- Sukuk – Medium and Long Term
- Rollover Murabaha – Medium Term
- Murabaha/Reverse Murabaha – Short Term

Sukuk by way of securitization of existing assets

■ **Definition:**

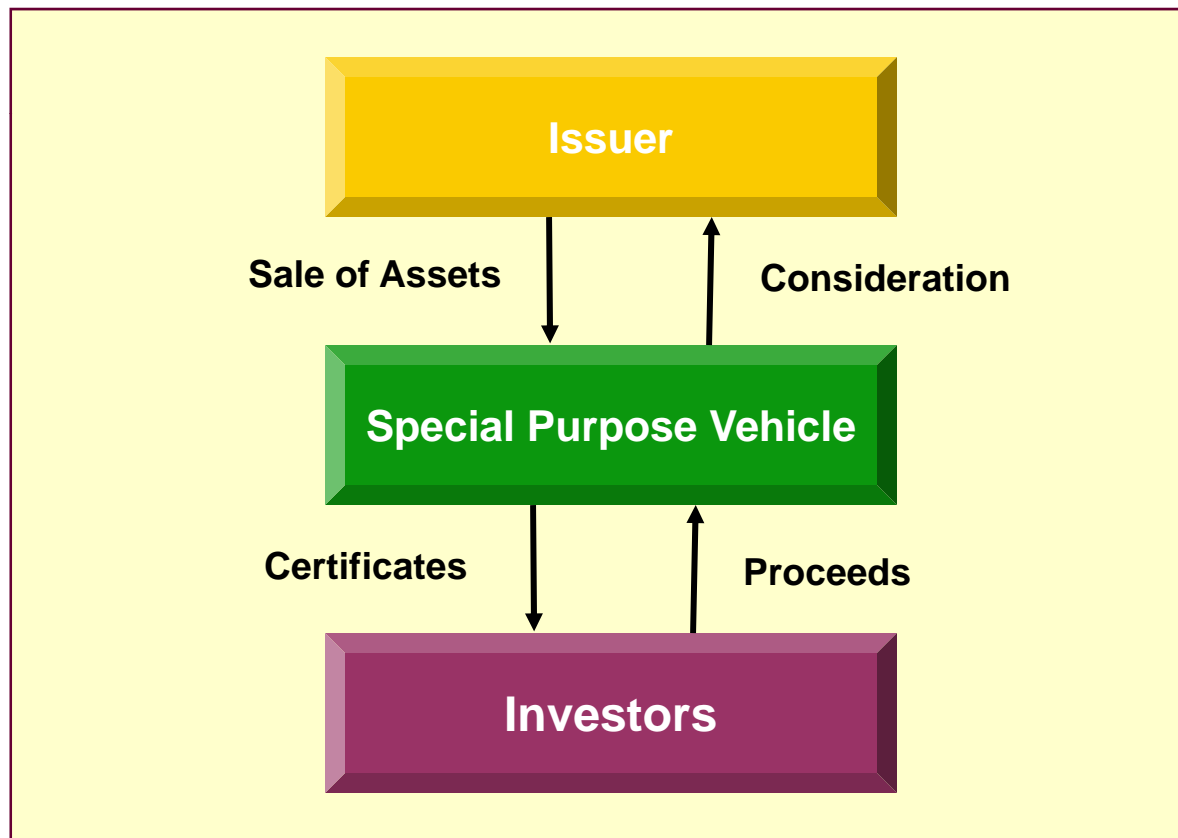
- A financial technique that pools assets for issuing financial paper for trading in the market.

■ **Basic Structure:**

- Sale by the originator of the pool of assets to a Special Purpose Vehicle (SPV).
- Issuance of certificates by the SPV to the investors.

Sukuk

■ Basic Sukuk Structure



Other parties involved

- Rating Agencies
- Paying Agent
- Financial Market
- Lead Managers/Underwriters/Placement Agents
- Trustee
- Legal Advisors
- Auditors

Benefits of Sukuk (Securitization) for the Investors

- Low risk investment arising from backing of a pool of assets coupled with other credit enhancement features embedded in the structure.
- Diversification of investments in a wide range of assets having a varied risk/return features and maturities.
- Participation in a growing Sukuk market.

Benefits of Sukuk (Securitization) to the Issuer

- Increased Liquidity.
- Risk Mitigation by Asset Diversification
- Efficient Asset Management
- Efficient Cash-flow Management
- Reducing Funding Costs
- Improving Rate of Return

Sukuk - Issues Involved

- Eligibility of Assets
- Selection/establishment of the SPV
- Ownership of the SPV
- Transfer/sale of assets
- Servicing/monitoring of the assets
- Legal Framework
- Credit Enhancement
- *Shari'ah* clearance
- Listing of the Sukuk
- Verification by the External Auditors
- Taxation
- Settlement

Eligibility of Assets for Sukuk Issuance

- The most important step for issuing a Sukuk based on existing assets is to determine the underlying pool of assets i.e. the issuer must possess a pool of assets on its balance sheet that are transferable to the investors.
- Flexibility in the assets pool to have a blend of *Ijara* and *Musharaka* (equity) assets and other *Shari'ah* compatible assets (e.g. *Murabaha* or *Istisna'a*)

Transfer of Assets Ownership to the SPV

- Transfer of assets' ownership to the SPV requires:
 - A clear definition of who the owners of the assets are?
 - A clear definition of who the buyers of the assets are?
 - A clear definition of the means of asset transfers.
- Limited Recourse legal relationship between the:
 - Sukuk certificate holders and the SPV (only proceeds from the trust assets)
 - SPV and the Seller of the assets (Pre-identified assets).
- Servicing/monitoring of the Assets is handled by the Trustee or by its agent (including the issuer in its capacity as an agent (*Wakeel*) of the Trustee).

Legal Framework – The SPV

- Sukuks are Trust Certificates backed by a portfolio of *Shari'ah* compatible assets.
- For legal, financial (risks and returns associated with the certificate), governance and transparency issues, the ownership of the portfolio of assets is transferred to an independent legal entity or a SPV.
- The SPV should be incorporated solely for the purpose of issuance and management of the Sukuk certificates in accordance with the Offering Circular.

Legal Framework - The SPV and The Legal Agreements

- The authorized and issued share capital of the SPV must be clearly indicated and fully paid up before the issuance of the Sukuk certificates.
- In any Sukuk issuance, there are several underlying agreements or transaction documents that must be put together, clearly explained and revealed in the offering circular.

Legal Framework – Some Basic Agreements

Original Seller/SPV:	Purchase Agreement
Asset User/Issuer:	Master <i>Ijara</i> /Leasing Agreement
SPV/Final Buyer:	Purchase Undertaking/Sale Undertaking
SPV (Trustee)	Declaration of Trust The Agency Agreement The Cost Undertaking Report of the Rating Agency Regulatory/Exchange clearance

Legal Framework – Governing Laws

- Governing Laws for different transaction or underlying agreements related to Sukuk certificates are usually structured as follows:
 - Governing Law for the underlying agreements related to the sukuk certificates is usually the English Law.
 - Governing Law in relation to the SPV's functions is usually the legal system of the domicile of the SPV.
- Format: Reg S & 144A

Legal Framework – Clearance & Settlement

- Clearance and Settlement Issues:
- Initial Settlement: Sukuk certificates are usually issued in global forms represented by the Global Certificates. Interests in the Global Certificates will be in book-entry form. Euroclear and Clearstream are usually the Settlement & Clearing systems for most issues.

Credit Enhancement

Credit enhancements are required to (a) reduce the risks to the Investors, (b) increase the rating of the Securities and thereby lower the costs to the issuer. Typical forms of credit enhancement are:

- Over-collateralization – transferring to the SPV, Asset Valuing more than required to pay the Securities.
- Early amortization option - if certain negative events occur, all payments from assets are applied to redeem the certificates.
- Cash collateral account – the issuer deposits funds in account with Trustee to be used if proceeds from Assets are not sufficient.
- Pledge of Securities – Additional securities provided by the issuer for the benefit of the Trust.
- Guarantee – guarantee of all payments by the issuer.
- Liquidity provider – in effect, a guarantee by the issuer (or its parent) or another entity for the payments due on the Securities.

Rating Issues

- Have the backing of a diversified pool of assets
- Past performance of assets pool (the assets pool should have a reasonably predictable cash flow and satisfactory repayment behavior).
- Necessary agreements and contracts should be in place
- Proper legal and recourse structures.
- Overall financial health of the issuer/its rating etc.

Types of Commonly Issued Sukuks

- Ijara
- Musharaka
- Convertible
- Murabaha
- Salam
- Istisna'

Issuance of Sukuk by IDB

Private Placements

S. No.	Amount In Million	Tenor	Maturity	Pricing
1	US\$ 138.5	3 years	14-Sep-12	3-months LIBOR + 20 bps
2	US\$ 100.0	3 years	26-Aug-12	6-months LIBOR + 35 bps
3	US\$ 50.0	3 years	16-Sep-12	6-months LIBOR + 35 bps
4	US\$ 500.0	10 years	20-Sep-20	3.25% pa Fixed

IDB International Sukuk

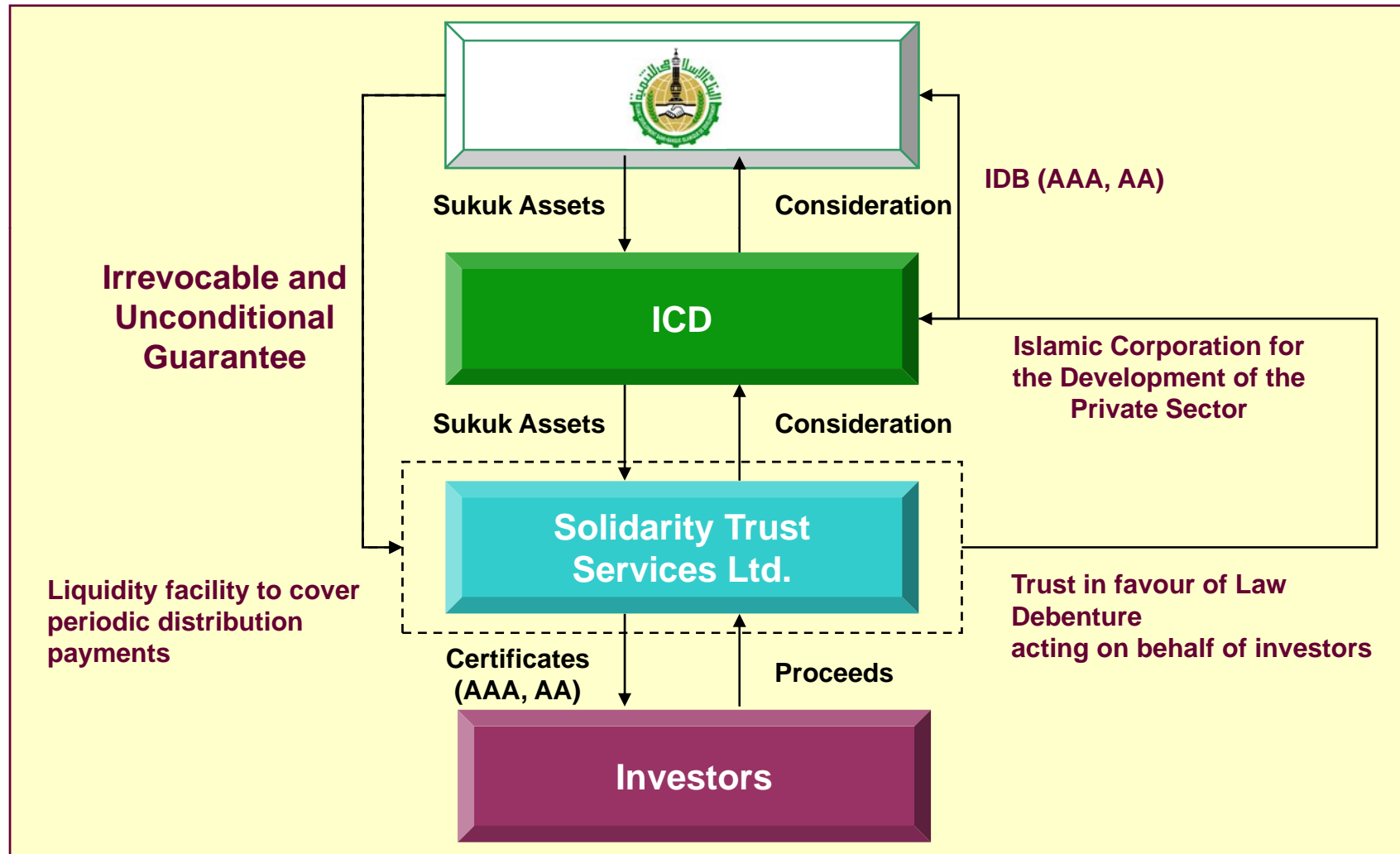
5	US\$ 400.0	5 years	12-Aug-08	3.625% pa fixed (Redeemed)
6	US\$ 500.0	5 years	22-Jun-10	6-months LIBOR + 12 bps (Redeemed)
7	US\$ 850.0	5 years	16-Sep-14	MS + 40 bps
				6m-LIBOR+31.5 bps)
8	US\$ 500.0	5 years	27-Oct-15	1,775% pa fixed

IDB Member Countries' Local Currency Sukuk

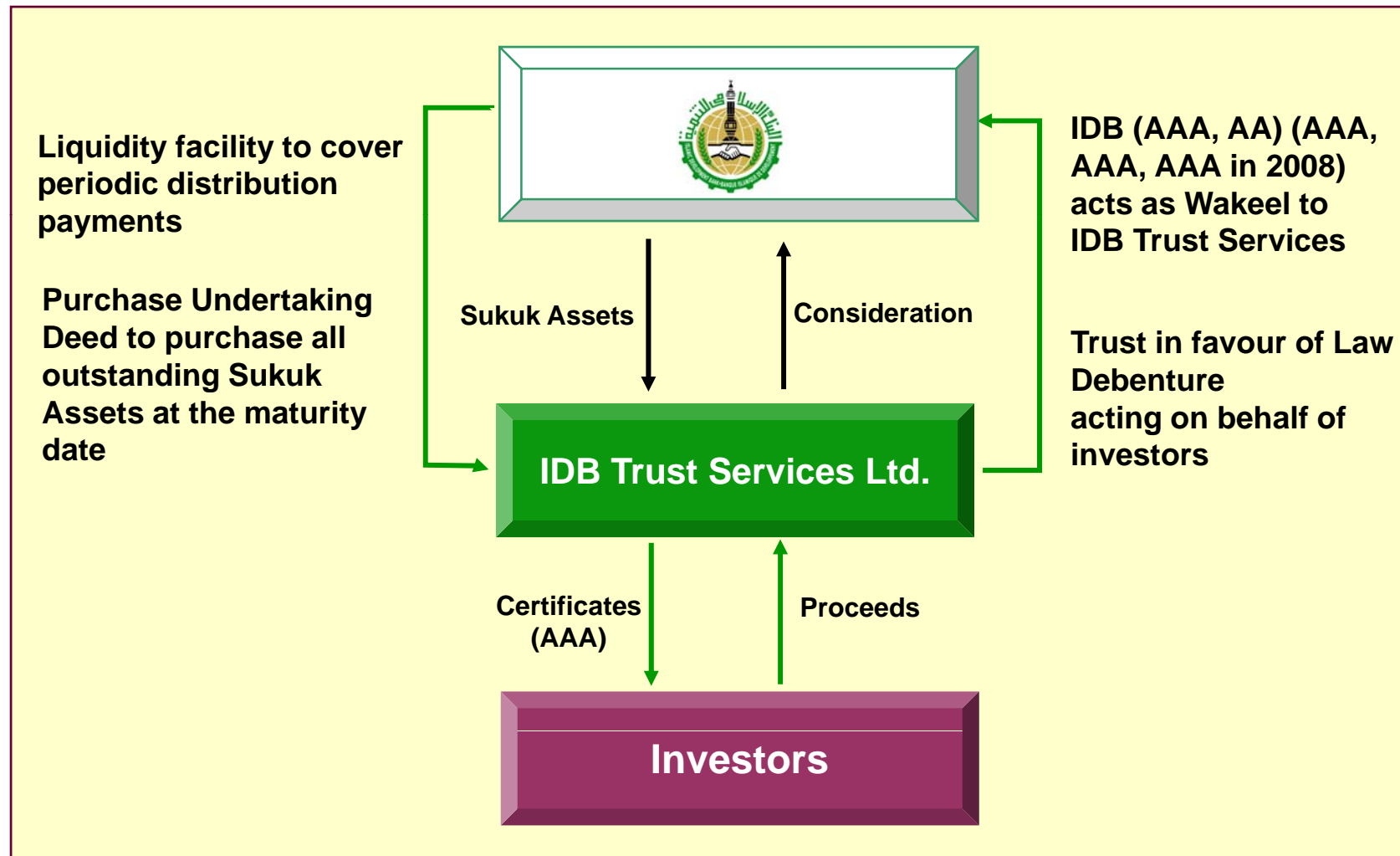
9	RM 300.0	5 years	20-Aug-13	4.58% pa fixed
10	RM 100.0	5 years	28-Mar-14	4.05% pa fixed

** Proceeds used for financing projects in Malaysia in local currency.*

IDB Sukuk Structure (Debut Sukuk)



IDB Sukuk Structure (Issuance under the MTN Programs)



BIS & Rating Agencies' Views

- BIS: **“Zero Risk Weighting”**,
under Basel II
- European Parliament: **“Zero Risk Weighting”**
- Standard & Poor's: **“AAA”**
- Moodys: and **“AAA”**
- FitchRatings: **“AAA”**

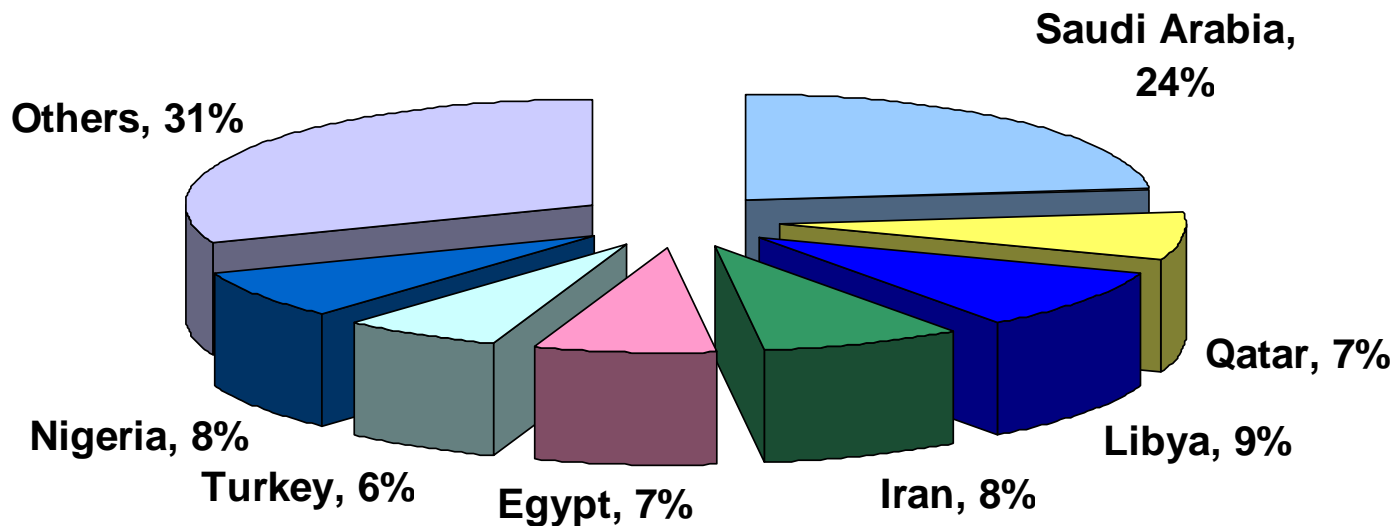
Capital Structure

IDB's Capital Structure – March 2011	ID (million)	US\$ (million)
Authorized Capital	30,000	47,466
Issued Capital	18,000	28,480
Paid-up Capital	4,093	6,476
Shareholders' Equity	5,508	8,715
Callable Capital	12,770	20,205

Note: 1 ID = 1.582211 US\$

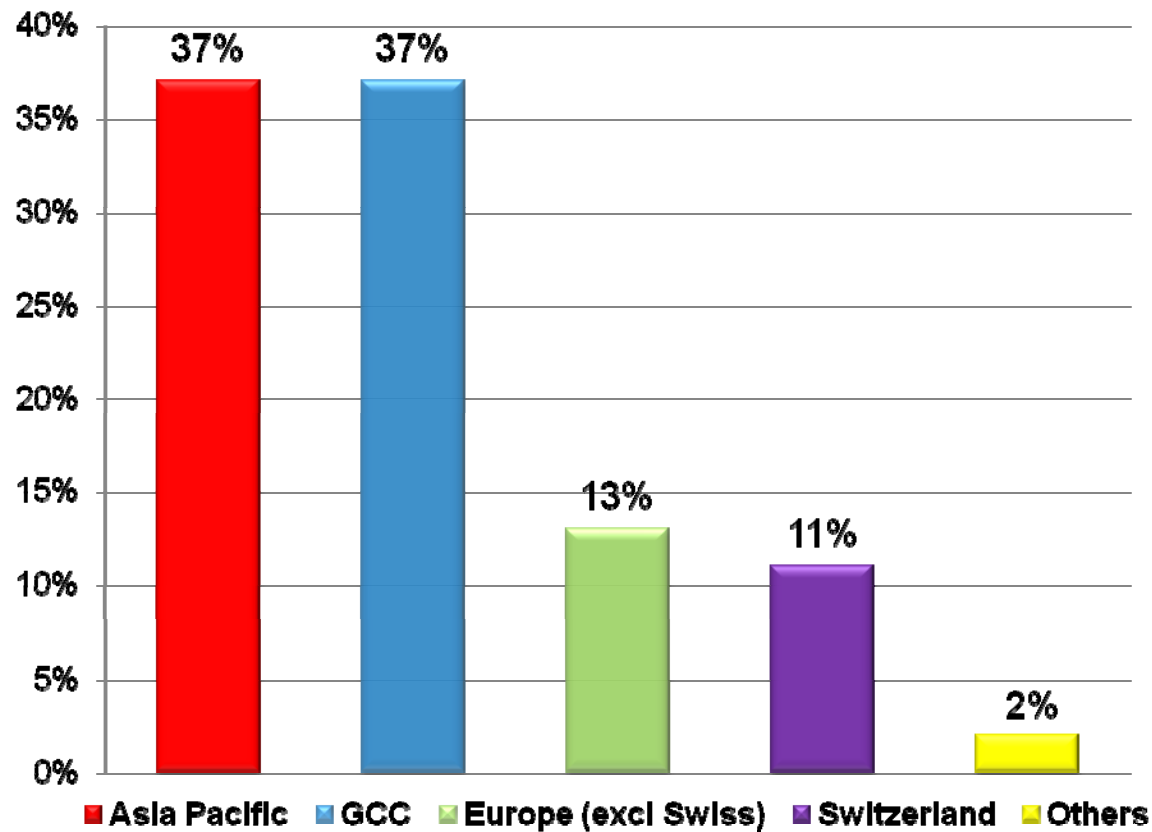
Largest Shareholder Countries

- Of IDB's 56 member countries, the largest shareholder is Saudi Arabia, holding over 25.73% of the paid up capital
- The top 7 members make up almost 69.84% of the total ownership of IDB most of which are major producers of fossil oil in the world.

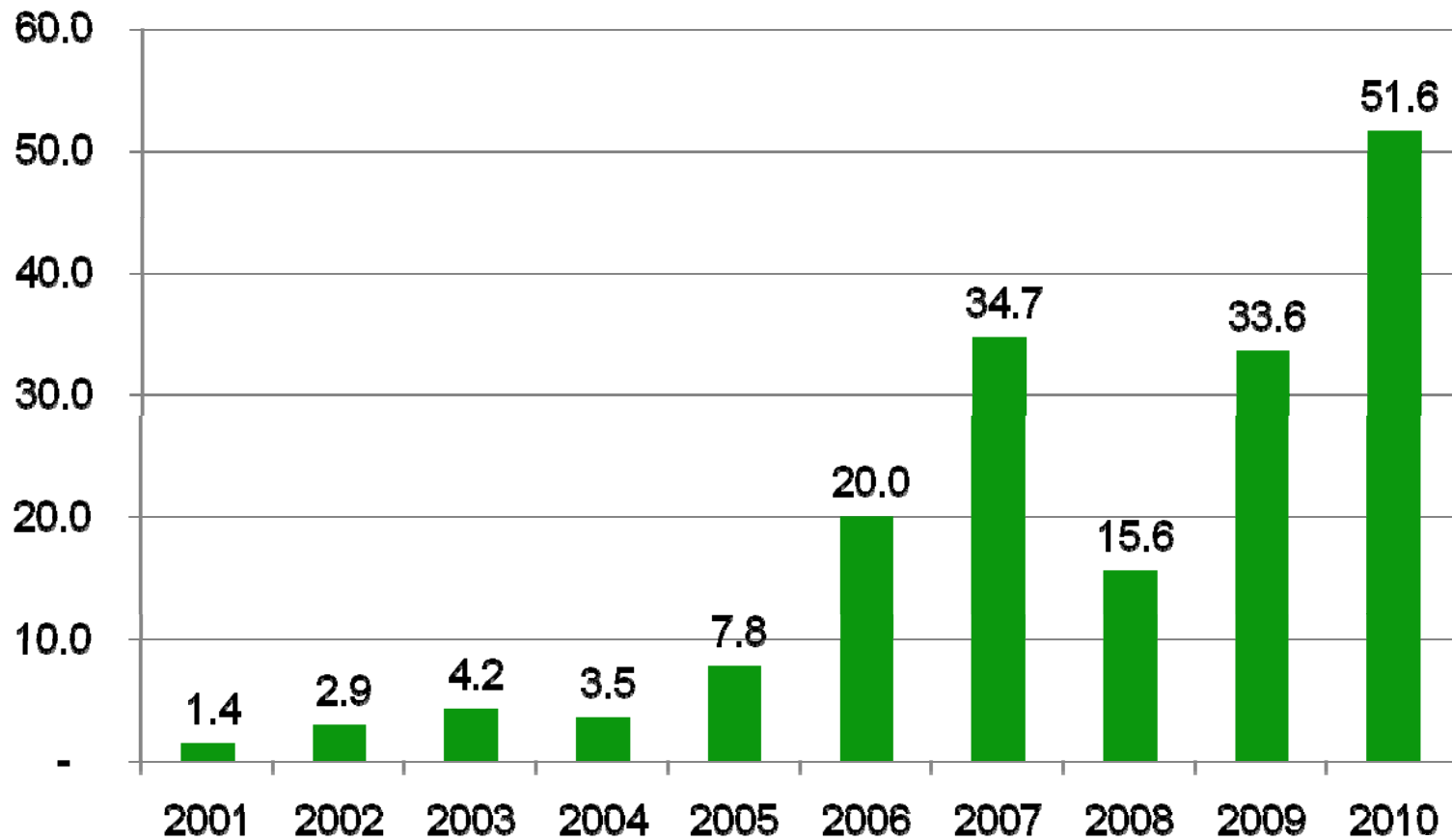


Note: Percentage based on subscribed capital

Key Investors of US\$ 850 Million Sukuk of IDB by Region



Global Sukuk Issuances



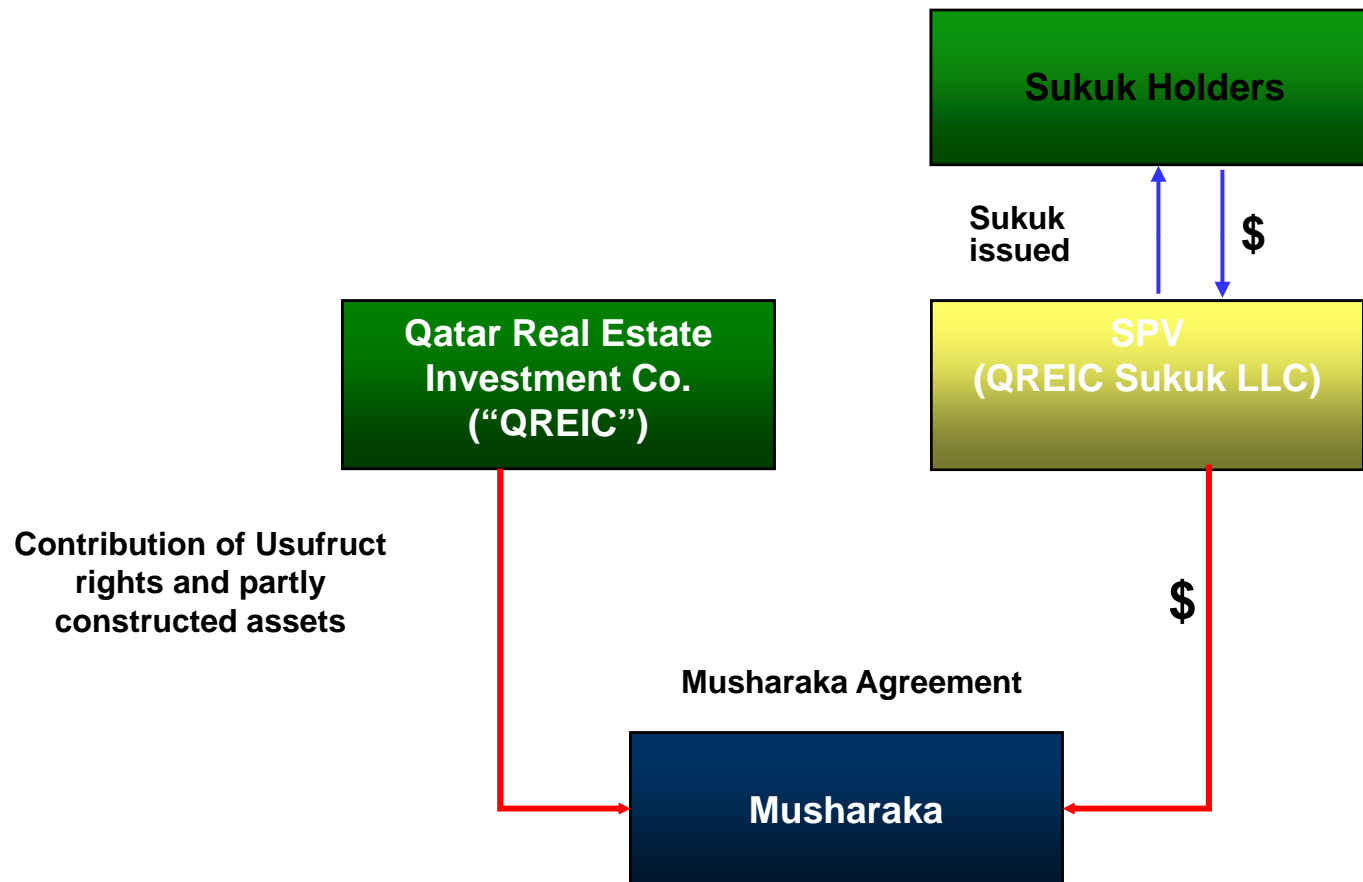
Amounts in US\$ billion



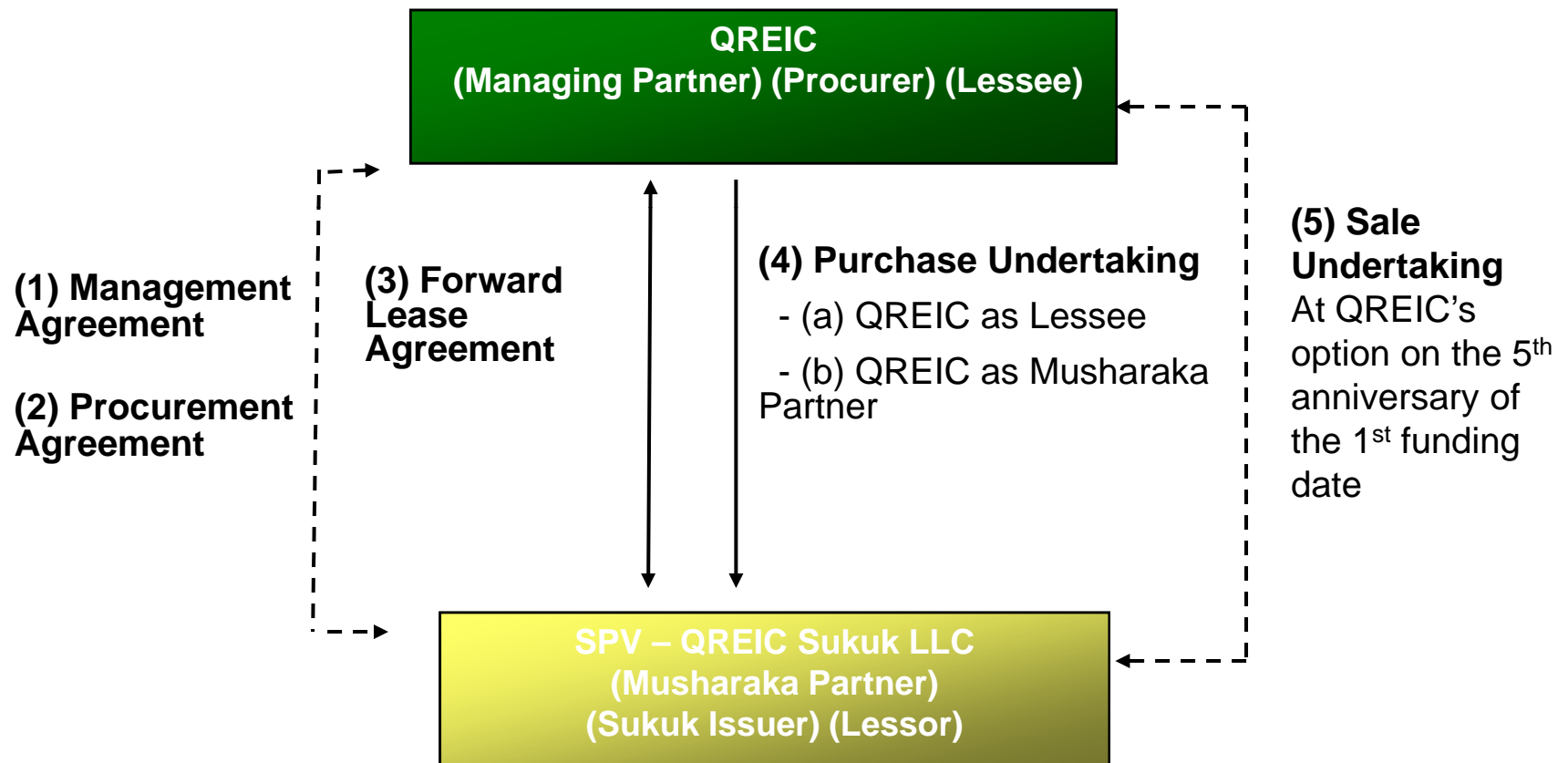
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Thank You

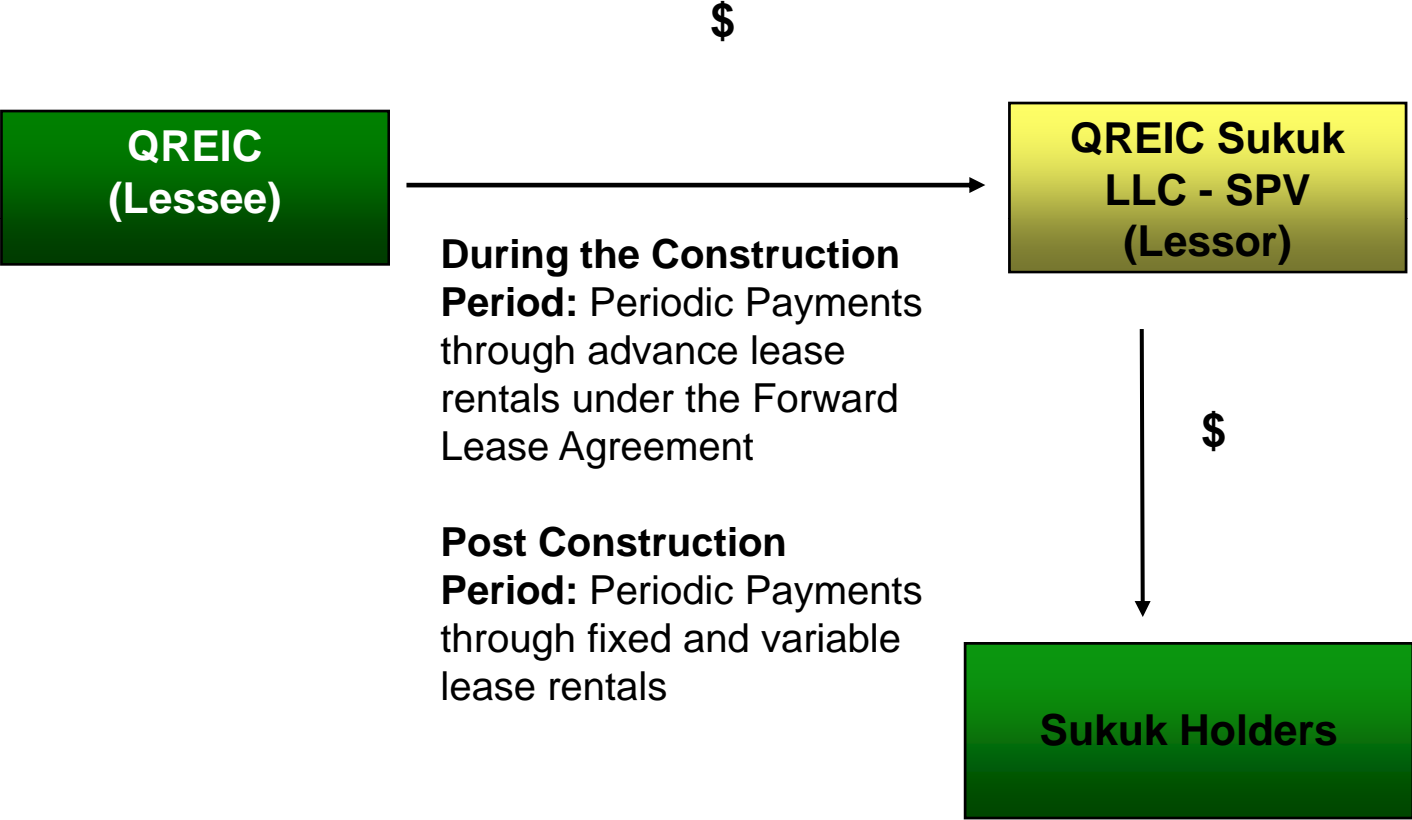
Musharaka Sukuk - Formation of Musharaka



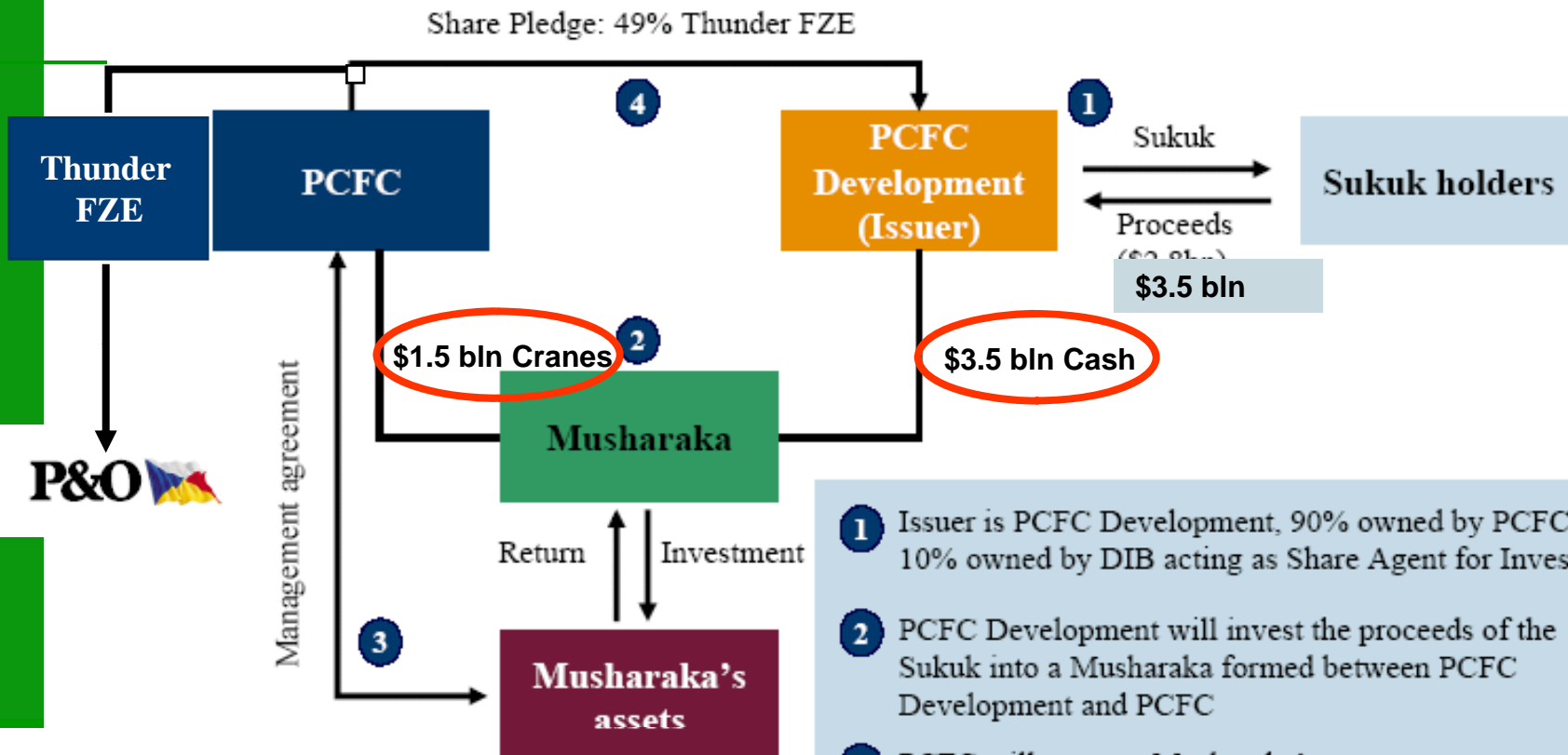
Musharaka Sukuk - Appointment of Managing Partner & Procurer & Fwd Lease Agreement



Musharaka Sukuk - Periodic Payments



Convertible Sukuk Structure



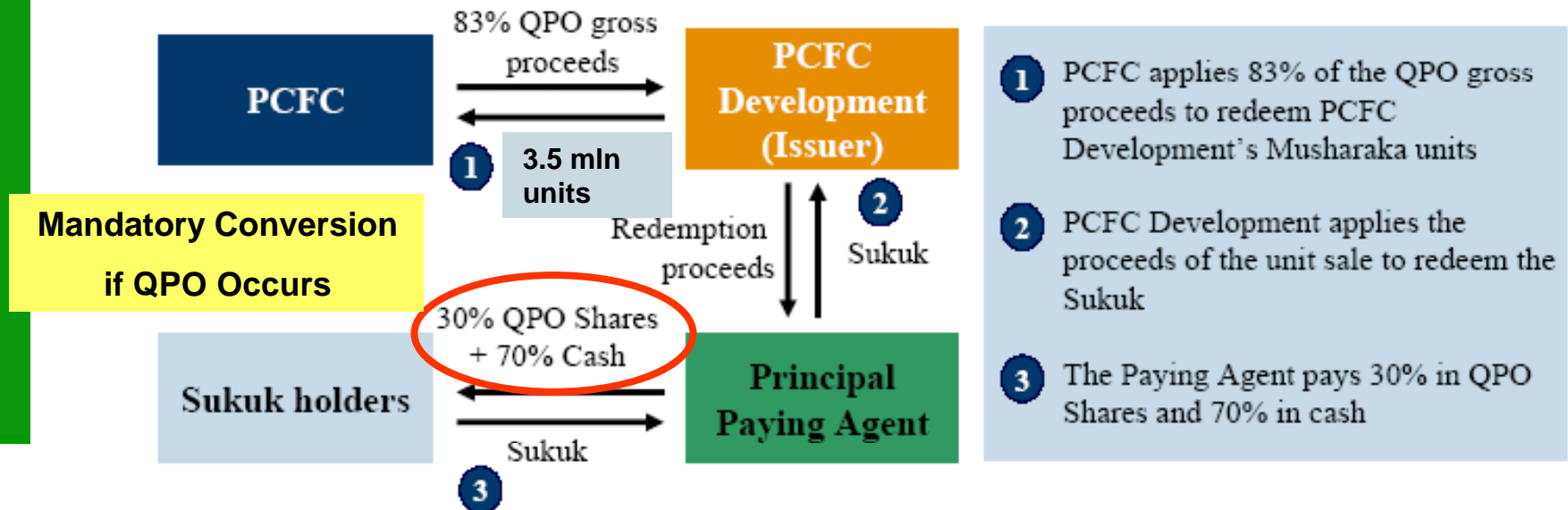
- 1 Issuer is PCFC Development, 90% owned by PCFC and 10% owned by DIB acting as Share Agent for Investors
- 2 PCFC Development will invest the proceeds of the Sukuk into a Musharaka formed between PCFC Development and PCFC
- 3 PCFC will manage Musharaka's assets, pursuant to the terms of a management agreement
- 4 PCFC will also enter into a purchase undertaking with PCFC Development and pledge 49% of the shares of Thunder FZE, the company that would acquire P&O

• If Musharaka profit is greater than the Distribution Amount, the surplus is distributed to the Managing Agent (PCFC) as incentive fees

• If Musharaka profit is less than the Distribution Amount, the Issuer can exercise the PCFC Purchase Undertaking as Dissolution Event

Convertible Sukuk Structure if QPO occurs

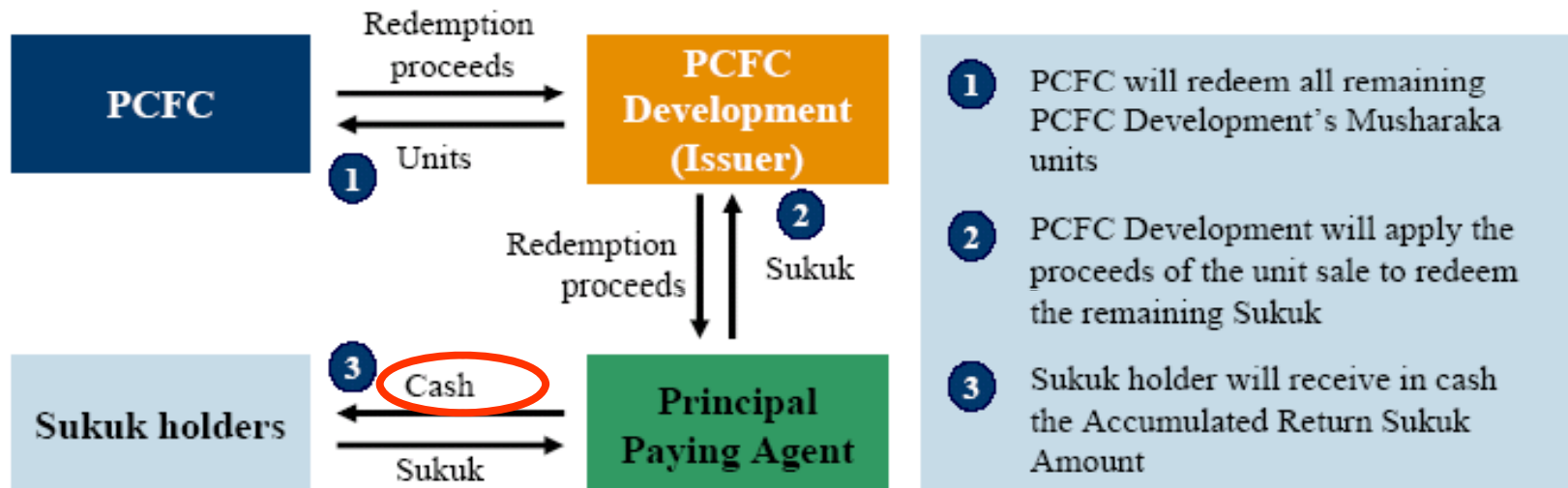
- In case of a Qualifying Public Offering of PCFC and/or subsidiaries (QPO), 83% of the QPO gross proceeds will be used to redeem the Sukuk
- Sukuk will be redeemed at their principal plus accretion in value, based on **7.125% pa**



Note: In case QPO proceeds are insufficient to redeem all the Sukuk, a partial redemption will take place. Several rounds of redemption may take place until all Sukuk are redeemed or mature

Convertible Sukuk Structure at Maturity

- Any outstanding amount at maturity will be redeemed at their principal plus accretion in value, based on an enhanced yield of 10.125% pa which is higher than QPO Yield 3%



- The same redemption mechanism will be used in case of a Dissolution event